

# LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS' PLAN 2 RETIREMENT BOARD

## Duty Disability Actuarial Reductions

May 26, 2004

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| <b>Issue</b>             | The pension benefits for LEOFF Plan 2 members who become disabled in the line of duty are subject to an actuarial reduction based on the member's age.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |
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| <b>Members Impacted</b>  | For purposes of HB 2418 in 2004 the Office of the State Actuary estimated that 12 LEOFF Plan 2 members per year become disabled in the line of duty. However, exact historical disability information for LEOFF 2 is not available.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          |
| <b>Current Situation</b> | A LEOFF Plan 2 member who becomes totally incapacitated for continued employment as a law enforcement officer or firefighter is eligible to receive a disability retirement benefit. The disability retirement benefit is actuarially reduced based on the difference between the member's age and age 53, the plan's normal retirement age. The actuarial reduction applies whether the disability is duty-related or not.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  |
| <b>History</b>           | HB 2418 in 2004 provided minimum duty disability benefits for LEOFF Plan 2 members. That legislation did not adjust the actuarial reduction for disability retirements.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
| <b>Example</b>           | <p><i>Hypothetical example:</i></p> <p>A law enforcement officer or firefighter who is age 43 with 15 years of service credit and an final average salary of \$45,000/year is totally incapacitated for continued employment. The member is eligible for a disability pension even though they do not meet the age and service requirements for normal retirement.</p> <p>The member's base pension is equal to 2% of their final average salary multiplied by their years of service. In this case, <math>2\% \times \\$45,000/\text{year} \times 15 =</math> a base pension of \$13,500/year or \$1125/month.</p> <p>The member's base pension is reduced by an actuarial factor determined by how far the member is from the age 53 normal retirement age. In this case, the member is ten years from normal retirement eligibility so the reduction factor is 0.43 and the member's base pension would be reduced to \$483.75/month.</p> |

## **Background Information and Policy Issues**

### **Comparison of Duty v. Non-Duty Benefits:**

The disability retirement benefits for LEOFF Plan 2 are provided in RCW 41.26.470 [see appendix A]. LEOFF Plan 2 members whose disability occurs in the line of duty are eligible for some benefits that are not available to members whose disability is not duty related. Specifically,

- The member may receive service credit for up to six months from the date of injury or illness; and
- The member may be entitled to a disability leave supplement from their employer equal to 50% of base monthly salary for periods of temporary total disability up to a maximum of six months; and
- The member is entitled to either withdraw 150% of their accumulated contributions and interest or receive a disability retirement pension that cannot be reduced below 10% of the member's average final salary.

### **Determination of Disability:**

The Department of Retirement Systems evaluates LEOFF Plan 2 disability retirement applications. The member must be totally incapacitated for employment by a LEOFF employer and the disabling injury or illness must be sustained in the course of employment in order to qualify for duty-related disability retirement benefits. The Department uses medical records and findings of the Department of Labor & Industries to determine whether the member's disabling condition was sustained in the course of employment.

### **Actuarial Benefit Reduction:**

The base pension formula for disability retirees is the same whether the disability is duty-related or not. The base formula is 2 percent multiplied by the member's final average salary multiplied by the member's years of service and actuarially reduced by the difference between the member's age at the time of disability and age 53.

- The member's final average salary is the average of the member's basic salary for the highest consecutive sixty months prior to retirement.
- The actuarial reduction factors are found in WAC 412-02-320 [see Appendix B].

The member's base pension may be further reduced at the member's option in order to provide a survivor benefit to a beneficiary such as the retiree's spouse or to pay premiums for health insurance.

### **Comparison to Other Public Pension Plans in Washington:**

LEOFF Plan 2 and the Plan 2/3 systems for PERS, TRS and SERS all have roughly the same disability benefit (2% x average final salary x years of service actuarially reduced by the member's age compared to normal retirement age) and the same statutory standard, "totally incapacitated for continued employment by an employer as determined by the Department of Retirement Systems."

LEOFF Plan 2 and the Plan 2/3 systems for PERS, TRS and SERS all use a 60-month period for determining final average salary. The effect of the actuarial reduction for the member's age

compared to normal retirement age is different between LEOFF 2 and the Plan 2/3 systems for PERS, TRS and SERS for two reasons:

- The normal retirement age in LEOFF 2 is age 53 compared to age 65 in the other Plan 2/3 systems; and
- The Plan 2/3 systems for PERS, TRS and SERS use a different actuarial reduction factor than that used for LEOFF Plan 2 [WAC 415-02-320(6)].

The Plan 1 retirement systems (PERS 1, TRS 1, and LEOFF 1) and the Washington State Patrol Retirement System (WSPRS) all have very different disability retirement benefits and different disability standards.

#### **Post-Retirement Employment:**

A LEOFF Plan 2 retiree, including a disability retiree, is not eligible to receive their pension if they are re-employed as a law enforcement officer or firefighter or if they are employed in an eligible position in the public employees' retirement system (PERS), the teachers' retirement system (TRS), or the school employees' retirement system (SERS). The retiree's benefits are reinstated when they terminate the employment that causes the benefits to be suspended.

A retiree's pension is not suspended if they return to work for a private employer, for a public employer in another state, or if the retiree returns to work in an ineligible position for a public employer in Washington.

#### **IRS Treatment of Duty-Related Disability Retirement Benefits:**

Duty-related disability retirement benefits may qualify for favorable federal income tax treatment if the benefits meet certain statutory requirements. Some of the key requirements are:

- The disabling injury or illness must have occurred as a result of the member's employment; and
- The benefit cannot be based on the member's service; and
- The benefit cannot be based on the member's age.

The base pension benefit in LEOFF Plan 2 does not qualify for favorable federal income tax treatment even if the disability is duty-related because the base pension is based on a member's years of service and may be actuarially reduced based on the member's age.

House Bill 2418 which was passed by the Legislature in 2004 established a minimum benefit for duty-related disabilities equal to 10% of the member's final average salary or 150% of the member's accumulated contributions and interest. This benefit qualifies for favorable income tax treatment under current law.

#### **Comparisons with other States:**

Duty-related disability benefits in police and fire plans around the nation typically fall into three categories:

- A minimum benefit based on the member's salary and unrelated to the member's age and/or service. The 10% minimum benefit in LEOFF Plan 2 is an example of this type of benefit.

- A pension based on the member's service which may or may not be reduced by the member's age. The base disability benefit in LEOFF Plan 2 is an example of this type of benefit.
- A special benefit for members who are extremely disabled. LEOFF Plan 2 does not have a benefit which falls into this category. The disability standard and benefit vary greatly from plan to plan in other states but an example of this type of benefit would be a lifetime benefit based on the member's salary and might include medical care for a member whose disability prevents all further employment in any capacity, public or private.

#### **Number of Members Affected:**

There have been very few disability retirements in LEOFF Plan 2 since the plan became effective in 1977. There are a number of possible reasons for this historical experience.

- Members who were not vested may have chosen to withdraw their accumulated contributions plus interest.
- Members who were already eligible for a service retirement would have received no additional retirement benefit from a disability retirement.
- Members with ten years of service who were not eligible for a service retirement may have preferred to withdraw 150% of their accumulated contributions and interest rather than take an actuarially-reduced pension.
- Members who were not eligible for a service retirement may have elected to defer retirement until normal retirement age rather than take an actuarially-reduced pension.

The Office of the State Actuary (OSA) estimated that 12 LEOFF Plan 2 members become disabled in the line of duty each year in the fiscal note for HB 2418 in 2004. OSA used historical experience in the State Patrol Retirement System and LEOFF Plan 1 to develop that estimate. The estimated number of duty-related disabilities for future legislation may differ from the estimates for HB 2418 depending on actual experience and the type of disability benefit that is proposed.

### **Policy Options**

- 1. Eliminate the actuarial reduction for a member's age**  
This approach would provide the member with their full earned pension in the event of duty-related disability by eliminating the actuarial reduction based on the difference between the member's age at the time of disability and the normal retirement age. The duty disability standard would remain unchanged. This approach would not allow for favorable federal income tax treatment.
- 2. Establish a special benefit for extreme disabilities**  
This approach would create a higher disability standard and provide a correspondingly higher level of benefits. This approach may allow for favorable federal income tax treatment.
- 3. Increase the minimum disability benefit**  
This approach would increase the 10% minimum benefit for duty-related disability retirement. This approach would allow for favorable federal income tax treatment.

The fiscal and administrative impacts of these options have not been determined for this introductory report.

## Appendix A

### RCW 41.26.470

(1) A member of the retirement system who becomes totally incapacitated for continued employment by an employer as determined by the director shall be eligible to receive an allowance under the provisions of RCW 41.26.410 through 41.26.550. Such member shall receive a monthly disability allowance computed as provided for in RCW 41.26.420 and shall have such allowance actuarially reduced to reflect the difference in the number of years between age at disability and the attainment of age fifty-three.

(2) Any member who receives an allowance under the provisions of this section shall be subject to such comprehensive medical examinations as required by the department. If such medical examinations reveal that such a member has recovered from the incapacitating disability and the member is no longer entitled to benefits under Title 51 RCW, the retirement allowance shall be canceled and the member shall be restored to duty in the same civil service rank, if any, held by the member at the time of retirement or, if unable to perform the duties of the rank, then, at the member's request, in such other like or lesser rank as may be or become open and available, the duties of which the member is then able to perform. In no event shall a member previously drawing a disability allowance be returned or be restored to duty at a salary or rate of pay less than the current salary attached to the rank or position held by the member at the date of the retirement for disability. If the department determines that the member is able to return to service, the member is entitled to notice and a hearing. Both the notice and the hearing shall comply with the requirements of chapter 34.05 RCW, the Administrative Procedure Act.

(3) Those members subject to this chapter who became disabled in the line of duty on or after July 23, 1989, and who receive benefits under RCW 41.04.500 through 41.04.530 or similar benefits under RCW 41.04.535 shall receive or continue to receive service credit subject to the following:

- (a) No member may receive more than one month's service credit in a calendar month.
- (b) No service credit under this section may be allowed after a member separates or is separated without leave of absence.
- (c) Employer contributions shall be paid by the employer at the rate in effect for the period of the service credited.
- (d) Employee contributions shall be collected by the employer and paid to the department at the rate in effect for the period of service credited.
- (e) State contributions shall be as provided in RCW 41.45.060 and 41.45.067.
- (f) Contributions shall be based on the regular compensation which the member would have received had the disability not occurred.
- (g) The service and compensation credit under this section shall be granted for a period not to exceed six consecutive months.
- (h) Should the legislature revoke the service credit authorized under this section or repeal this section, no affected employee is entitled to receive the credit as a matter of contractual right.

(4)(a) If the recipient of a monthly retirement allowance under this section dies before the total of the retirement allowance paid to the recipient equals the amount of the accumulated contributions at the date of retirement, then the balance shall be paid to the member's estate, or such person or persons, trust, or organization as the recipient has nominated by written designation duly executed and filed with the director, or, if there is no such designated person or persons still living at the time of the recipient's death, then to the surviving spouse, or, if there is neither such designated

person or persons still living at the time of his or her death nor a surviving spouse, then to his or her legal representative.

(b) If a recipient of a monthly retirement allowance under this section died before April 27, 1989, and before the total of the retirement allowance paid to the recipient equaled the amount of his or her accumulated contributions at the date of retirement, then the department shall pay the balance of the accumulated contributions to the member's surviving spouse or, if there is no surviving spouse, then in equal shares to the member's children. If there is no surviving spouse or children, the department shall retain the contributions.

(5) Should the disability retirement allowance of any disability beneficiary be canceled for any cause other than reentrance into service or retirement for service, he or she shall be paid the excess, if any, of the accumulated contributions at the time of retirement over all payments made on his or her behalf under this chapter.

(6) A member who becomes disabled in the line of duty, and who ceases to be an employee of an employer except by service or disability retirement, may request a refund of one hundred fifty percent of the member's accumulated contributions. Any accumulated contributions attributable to restorations made under RCW 41.50.165(2) shall be refunded at one hundred percent. A person in receipt of this benefit is a retiree.

(7) A member who becomes disabled in the line of duty shall be entitled to receive a minimum retirement allowance equal to ten percent of such member's final average salary. The member shall additionally receive a retirement allowance equal to two percent of such member's average final salary for each year of service beyond five, and shall have the allowance actuarially reduced to reflect the difference in the number of years between age at disability and the attainment of age fifty-three. An additional benefit shall not result in a total monthly benefit greater than that provided in subsection (1) of this section.

## Appendix B

### WAC 415-02-320

(5) Table - Early retirement factors (ERF) for these systems/plans: LEOFF Plan 2, WSP Plan 2, PERS Plan 1, TRS Plan 1, and WSP Plan 1 and 2 vested/terminated members:

| Yrs Early | Month 0 | Month 1 | Month 2 | Month 3 | Month 4 | Month 5 | Month 6 | Month 7 | Month 8 | Month 9 | Month 10 | Month 11 |
|-----------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|----------|----------|
| 0         | 1.000   | .9933   | .9866   | .9799   | .9732   | .9665   | .9598   | .9531   | .9464   | .9397   | .9330    | .9263    |
| 1         | .9200   | .9133   | .9066   | .8999   | .8932   | .8865   | .8798   | .8731   | .8664   | .8597   | .8530    | .8463    |
| 2         | .8400   | .8333   | .8266   | .8199   | .8132   | .8065   | .7998   | .7931   | .7864   | .7797   | .7730    | .7663    |
| 3         | .7600   | .7558   | .7516   | .7474   | .7432   | .7390   | .7348   | .7306   | .7264   | .7222   | .7180    | .7138    |
| 4         | .7100   | .7058   | .7016   | .6974   | .6932   | .6890   | .6848   | .6806   | .6764   | .6722   | .6680    | .6638    |
| 5         | .6600   | .6558   | .6516   | .6474   | .6432   | .6390   | .6348   | .6306   | .6264   | .6222   | .6180    | .6138    |
| 6         | .6100   | .6058   | .6016   | .5974   | .5932   | .5890   | .5848   | .5806   | .5764   | .5722   | .5680    | .5638    |
| 7         | .5600   | .5558   | .5516   | .5474   | .5432   | .5390   | .5348   | .5306   | .5264   | .5222   | .5180    | .5138    |
| 8         | .5100   | .5067   | .5034   | .5001   | .4968   | .4935   | .4902   | .4869   | .4836   | .4803   | .4770    | .4737    |
| 9         | .4700   | .4667   | .4634   | .4601   | .4568   | .4535   | .4502   | .4469   | .4436   | .4403   | .4370    | .4337    |
| 10        | .4300   | .4267   | .4234   | .4201   | .4168   | .4135   | .4102   | .4069   | .4036   | .4003   | .3970    | .3937    |
| 11        | .3900   | .3867   | .3834   | .3801   | .3768   | .3735   | .3702   | .3669   | .3636   | .3603   | .3570    | .3537    |
| 12        | .3500   | .3467   | .3434   | .3401   | .3368   | .3335   | .3302   | .3269   | .3236   | .3203   | .3170    | .3137    |
| 13        | .3100   | .3083   | .3066   | .3049   | .3032   | .3015   | .2998   | .2981   | .2964   | .2947   | .2930    | .2913    |
| 14        | .2900   | .2883   | .2866   | .2849   | .2832   | .2815   | .2798   | .2781   | .2764   | .2747   | .2730    | .2713    |
| 15        | .2700   | .2683   | .2666   | .2649   | .2632   | .2615   | .2598   | .2581   | .2564   | .2547   | .2530    | .2513    |
| 16        | .2500   | .2483   | .2466   | .2449   | .2432   | .2415   | .2398   | .2381   | .2364   | .2347   | .2330    | .2313    |
| 17        | .2300   | .2283   | .2266   | .2249   | .2232   | .2215   | .2198   | .2181   | .2164   | .2147   | .2130    | .2113    |
| 18        | .2100   | .2092   | .2084   | .2076   | .2068   | .2060   | .2052   | .2044   | .2036   | .2028   | .2020    | .2012    |
| 19        | .2000   | .1992   | .1984   | .1976   | .1968   | .1960   | .1952   | .1944   | .1936   | .1928   | .1920    | .1912    |
| 20        | .1900   | .1892   | .1884   | .1876   | .1868   | .1860   | .1852   | .1844   | .1836   | .1828   | .1820    | .1812    |
| 21        | .1800   | .1792   | .1784   | .1776   | .1768   | .1760   | .1752   | .1744   | .1736   | .1728   | .1720    | .1712    |
| 22        | .1700   | .1692   | .1684   | .1676   | .1668   | .1660   | .1652   | .1644   | .1636   | .1628   | .1620    | .1612    |
| 23        | .1600   | .1592   | .1584   | .1576   | .1568   | .1560   | .1552   | .1544   | .1536   | .1528   | .1520    | .1512    |
| 24        | .1500   | .1492   | .1484   | .1476   | .1468   | .1460   | .1452   | .1444   | .1436   | .1428   | .1420    | .1412    |
| 25        | .1400   | .1392   | .1384   | .1376   | .1368   | .1360   | .1352   | .1344   | .1336   | .1328   | .1320    | .1312    |
| 26        | .1300   | .1292   | .1284   | .1276   | .1268   | .1260   | .1252   | .1244   | .1236   | .1228   | .1220    | .1212    |
| 27        | .1200   | .1192   | .1184   | .1176   | .1168   | .1160   | .1152   | .1144   | .1136   | .1128   | .1120    | .1112    |
| 28        | .1100   | .1092   | .1084   | .1076   | .1068   | .1060   | .1052   | .1044   | .1036   | .1028   | .1020    | .1012    |
| 29        | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000    | .1000    |
| 30        | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000    | .1000    |
| 31        | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000    | .1000    |
| 32        | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000    | .1000    |
| 33        | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000    | .1000    |
| 34        | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000    | .1000    |
| 35        | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000    | .1000    |
| 36        | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000    | .1000    |
| 37        | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000    | .1000    |
| 38        | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000    | .1000    |
| 39        | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000    | .1000    |
| 40        | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000   | .1000    | .1000    |